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Miles-High Disregard

Airlines off base on fuel costs.

By Jeb Hensarling

Pontificating without facts is a behavior often most often associated with politicians. Yet, as oil prices continue to rise, some airlines are doing just that by overlooking the facts and in the process misleading their customers.

Recently, the "Coalition to Stop Oil Speculation," a lobbying group of 12 major airlines, formed with support from the Air Transport Association of America. Millions of e-mails were sent to passengers urging them to clamp down on commodities investors — disparaged as "speculators."

The airlines have clearly been hurt badly by our nation's energy woes, but to lay blame on investors is off the mark. Energy investors represent a timely scapegoat for the airline industry, which is currently coming under fire from passengers angered by new fees, spotty service, limited flights, and increased fares. When it comes to high oil prices, there is no doubt that there is plenty of blame to go around. But the chances that "speculators" are the true culprit are about equal to the chance that your flight arrives at its destination on schedule.

The airlines claim that "speculators" (again, think "investors") flood the market, artificially escalating oil prices to unrealistic levels. The reality is that commodities investments are not based on finger-in-the-wind guessing; but on analyses of trends in supply and demand. If investors see trends pointing toward increasing world demand (skyrocketing demand from India and China) and constrained supply (restricting exploration for American energy, limiting government procurement of unconventional fuels from North America, and constraining American refinery capacity), they are likely to bet on price escalation. Conversely, an actual increase in supply would cause prices to fall. Oil prices would drop immediately on the futures market with the allowance of drilling in ANWR, well before any oil is extracted. No matter what the bet, the reality is that any investor can only buy oil futures if there is another willing to sell it. In each circumstance that an investor bets on a price increase, there is an investor betting on a price decrease.

If the airlines, or Democrats, are to be believed, one would assume that "speculators" are characters out of a Dickens novel, seeking evil ways to profit on the back of the struggling working class. It turns out that these speculators are, in many cases, the working class. Since 2003, investments in commodities have increased from $13 billion to $260 billion. Among the largest investors, or "speculators," are pension funds. That's right, if you have a pension, there's a good chance that you are a "speculator."

Of course the truth is that investors have no inherent incentive to push prices upward, and when an investor guesses wrong, he will lose money. There is no greater benefit with a bet that commodity prices will go up than a bet that they will go down. In fact, if a company purchases the future right to buy oil at $120 a barrel and it instead sells for $100, the option becomes worthless. Southwest Airlines, in particular, should be very familiar with this process, as their decision to enter into long-term fuel hedge contracts years ago enables them to purchase oil at the equivalent of $51-a-barrel through 2009 while most of their competitors pay far more.

If the airlines are right and the facts wrong, maybe Congress needs to “do something” about “speculators.” Perhaps Congress could restrict investment in the airlines by prohibiting anyone that “speculated” on their value from buying stock and prohibit the airlines themselves from speculating on the cost of energy or other commodities. Perhaps passengers should not purchase tickets ahead of time, since purchasing a ticket in advance hoping that it might be cheaper than the day of the flight is a form of “speculation.” I would obviously oppose such a regulatory heavy hand, but I imagine that under the airlines’ logic, others in Congress would be quite sympathetic.

If the goal is to spur effective government action to help ease pressures in the oil commodity market, the airlines should work to benefit their passengers and mobilize their political muscle behind efforts to lift restrictions on exploration for energy off our shores, in the intermountain West, and in arctic Alaska. They should call for a reduction in the number of boutique fuels and an expansion of domestic refining capacity. And they should emphasize the importance of renewable energy and alternative technologies like coal to liquids, which are clearly the future. These common sense actions would increase global energy production and immediately send price-reduction signals to the futures markets. It’s all about supply and demand.

As a frequent flyer who has a high level of satisfaction with my airline of choice, it is clear that many airlines know much more about what it takes to pilot a plane than what it takes to power one economically. Let’s hope they figure it out soon.

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